CLIFFORD CHANCE

Briefing note

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AIFMD: ESMA consults on segregation requirements

The European Securities and Markets Authority (ESMA) has launched a consultation on asset segregation requirements under the Alternative Investment Fund Managers Directive (AIFMD). The consultation sets out ESMA's proposals for possible guidelines regarding the asset segregation requirements in case of delegation of safe-keeping duties by the appointed depositary of an alternative investment fund (AIF).

ESMA is seeking feedback on two possible options:

- a delegated third party holding assets for multiple depositary clients would not be required to have separate accounts for the AIF assets of each of the delegating depositaries; and
- the account on which the AIF's assets are to be kept by the delegated third party may only comprise assets of the AIF and assets of other AIFs of the same delegating depositary. Assets of AIFs of other depositary clients would have to be kept in separate accounts.

Comments are due by 30 January 2015 and ESMA will consider the feedback with a view to finalising guidelines and publishing a final report in Q2 2015.

BRRD: EBA consults on minimum requirement for own funds and eligible liabilities

The European Banking Authority (EBA) has published a consultation paper on draft regulatory technical standards (RTS) specifying the minimum requirement for own funds and eligible liabilities (MREL) under the Bank Recovery and Resolution Directive (BRRD). The BRRD sets out the requirement for institutions to meet MREL requirements in order to ensure the effectiveness of bail-in or other resolution tools. MREL is to be set on a case-by-case basis by resolution authorities and the draft RTS further specify the minimum criteria for resolution authorities in determining MREL to ensure convergence across Member States. The draft RTS are compatible with the proposed term sheet for Total Loss Absorbing Capacity (TLAC) for Global Systemically Important Institutions (G-SIIs) put forward by the Financial Stability Board (FSB).

The RTS also clarify how an institution's capital requirements should be linked to the amount of MREL needed to absorb losses and, where necessary, recapitalise a firm after resolution and any additional MREL required to implement the institution's resolution plan. The draft RTS also consider the effect of the Deposit Guarantee Scheme (DGS) contributions to the cost of resolution.

The draft RTS also propose that resolution authorities should identify as systemic those institutions that are identified as G-SIIs or Other Systemically Important Institutions (O-SIIs) for the purposes of the Capital Requirements Directive and Regulation (CRD 4/CRR). For such institutions, resolution authorities should consider the potential need to access the resolution financing arrangement if a resolution relying solely on the institution's own resources is not possible.

Comments on the consultation are due by 27 February 2015.

EU Council approves regulation on insolvency proceedings (recast)

The EU Council (Justice and Home Affairs) has approved a political agreement reached with the EU Parliament following trialogue discussions concerning the Regulation on insolvency proceedings (recast), which will replace the existing Regulation (EC) No 1346/2000 on insolvency proceedings that has applied since 31 May 2002. The recast Regulation is intended to improve the efficiency and effectiveness of cross-border insolvency, benefit creditors and debtors, facilitate the survival of businesses and present a second chance for entrepreneurs, and the key changes include:

- an expanded scope beyond the liquidation proceedings already covered by the current legislation to cover a range of commercial and personal insolvency proceedings;
- further clarification on the concept of centre of main interest (COMI) to increase legal certainty;
- new rules relating to secondary proceedings and specific guidance on the circumstances under which they may be postponed or refused;
- interconnection of insolvency registers via the European e-Justice Portal to enhance access to information and prevent the opening of parallel proceedings; and
- a new framework of procedural rules for insolvency proceedings concerning different entities within a group of companies.

The approved rules will be put before the Council of Ministers in March 2015 for formal adoption and then the EU Parliament's Legal Affairs Committee and Plenary in April or May 2015 for formal adoption. Once adopted, the Regulation will be published in the Official Journal and it will apply twenty four months following its entry into force.

PSD 2: EU Council Presidency publishes compromise text

The Presidency of the EU Council has published a compromise text on the proposal for a second Payment Services Directive (PSD 2) to repeal the current Directive 2007/64/EC. Alongside the compromise text, a report on the state of play of the negotiations on the proposal has also been published.

Basel Committee reports on Basel III implementation in EU and US

The Basel Committee for Banking Supervision (BCBS) has published its assessments of the implementation of the Basel III regulations in the EU and in the United States. The reports are part of BCBS' ongoing Regulatory Consistency Assessment Programme (RCAP) which is intended to promote the full and consistent adoption of the Basel framework by identifying jurisdiction-specific regulations for internationally active banks that are not convergent with the letter and spirit of the Basel standards. The RCAP then assesses rules against a four-grade categorisation to identify compliant, largely compliant, materially non-compliant and non-compliant rules.

The BCBS assessed the overall EU regime to be materially non-compliant with the intended minimum standards under the Basel III framework. It found eight of fourteen assessment components to be compliant and a further four were categorised as largely compliant, but the BCBS also identified important divergences in relation to the EU frameworks for:

- the internal ratings-based (IRB) approach for credit risk, which was categorised as materially non-compliant; and
- the credit valuation adjustment (CVA) exemptions for certain derivatives exposures, which was assessed to be non-compliant.

The BCBS assessed the overall US regime to be largely compliant with the intended minimum standards under the Basel III framework. The BCBS found seven of thirteen assessment components to be compliant and a further four were categorised as largely compliant, but the BCBS also identified important divergences in relation to:

- the securitisation framework, relating in particular to risk-weighted asset (RWA) outcomes; and
- the standardised approach for market risk.

The BCBS assessed the US framework in both of these areas to be materially non-compliant. In other areas, the BCBS identified potential material deviations, including the US implementation of the internal ratings-based (IRB) approach for credit risk. As such, the BCBS recommends reassessment of some of the deviations identified at post-RCAP annual follow-ups to monitor the materiality of certain deviations.

FCA consults on guidance on market conduct compliance for MTFs

The Financial Conduct Authority (FCA) has launched a consultation (GC 14/9) on general guidance relating to compliance with the FCA Handbook's market conduct standards for multilateral trading facilities (MTFs) found in MAR 5, which considers, in particular, MAR 5.3.1 on trading process requirements. The FCA has released a Dear CEO Letter and FCA Good Practice Observations on compliance with the rules.

Comments on the proposed guidance are due by 16 January 2015.

Entry into force of new law on security interests postponed

In July 2013 Belgium adopted a new law on security interests which seeks to modernise the legal framework for security interests and, in particular, to allow for inventory security to be perfected without dispossession. The law was meant to enter into force on 1 December 2014 at the latest, but the Belgian Parliament has now postponed the date of entry into force until 1 January 2017 at the latest.

Single Supervisory Mechanism: CSSF issues new circular on communication regime for significant entities

The Luxembourg financial sector supervisory authority, the Commission de Surveillance du Secteur Financier (CSSF), has issued a new circular (14/596) on the communication regime under the Single Supervisory Mechanism (SSM) for significant entities and the repeal of the VISA procedure for published annual accounts.

The circular is intended to make banks aware of the new communication regime between significant banks and the different authorities in charge of prudential supervision following the introduction of the SSM on 4 November 2014.

Article 95 of the SSM Framework Regulation requires that all requests, notifications or applications relating to the exercise of the tasks conferred to the European Central Bank (ECB) shall be addressed directly to the ECB. The circular states that significant entities and their subsidiaries should therefore send all communications to the addresses communicated to them by the ECB in August 2014. The circular further lists the exceptions to this principle under the SSM Framework Regulation where communication continues to take place directly between the credit institution and the CSSF (authorisations, passporting, acquisition of qualifying holdings, fit-and-proper assessments for managers, financial and prudential reporting) without prejudice to direct communication that may take place between the ECB granting the authorisations and the bank or applicant.

The CSSF recommends that any communication by a significant entity is made in English.

The circular finally abolishes the VISA procedure for published annual accounts for all credit institutions (both significant and less significant).

Polish Ministry of Finance proposes amendment to Act on Regulation of Financial Market

The Polish Ministry of Finance has published a proposal for an amendment to the Act on the Regulation of the Financial Market. The proposal provides for the following changes:

- broadening the powers of the Polish Financial Supervision Authority (PFSA) to conduct investigations into entities suspected of operating without a licence to cover all sectors of the financial market;
- introducing more severe criminal sanctions for collecting other people's funds without a permit for use involving risk;
- introducing statutory requirements which are a condition for business activity being the granting of consumer loans from the lender's own funds;
- limiting the potential for charging excessive fees, commissions and interest under loan and credit facility agreements; and
- defining rules with regard to access to, providing and exchanging information about consumer loans granted by banks and shadow banks.

The proposal is currently at the interdepartmental and public consultation stage.

Polish Financial Supervision Authority sets out position on dividend policy

The Polish Financial Supervision Authority (KNF) has adopted a position on the dividend policy of banks, insurance and reinsurance companies, general pension societies, brokerage houses and investment fund associations in the year 2015. The KNF attaches particular importance to banks which have an important share in the deposits market in Poland maintaining a sufficiently high level of capital.

FINMA publishes circulars on leverage ratio and disclosure

The Swiss Financial Market Supervisory Authority (FINMA) has published two circulars to implement Basel III international banking standards.

The new FINMA circular 2015/3 'Leverage ratio – banks' prescribes calculation rules for assessing total exposure for the leverage ratio.

A large number of respondents participated in the consultation on both circulars. Generally, they approved the introduction of the leverage ratio in line with international standards. Certain rules, however, such as the treatment of special purpose entities or the inclusion of all liquid assets in the total exposure were considered to be either too conservative or too complicated. As regards disclosure of the leverage ratio, the amount of detail and the implementation date provided reason for discussion.

The revised FINMA circular 2008/22 'Disclosure – banks' includes Basel III rules which require the disclosure of the leverage ratio and the liquidity coverage ratio by banks.

Under the current capital adequacy regulations, FINMA must apply Basel standards to all banks. This requires that for the Swiss standard approach a multiplier is used to calculate loan equivalents (exposure values) for derivatives in order to achieve equivalence with the Basel minimum standards. FINMA had proposed a multiplier of 2 that was regarded as too high. It has now been changed to 1.5.

As regards disclosure of the liquidity coverage ratio, FINMA will adopt the principle of materiality proposed by the industry for all non-systemically important banks. Those banks are not obliged to report on all qualitative points under the Basel III rules, but must do so for the points relevant to the bank itself. Moreover, systemically important banks may now use a risk-based approach for the daily LCR calculation. Instead of a daily calculation including all components, volatile components must be updated daily and less volatile components weekly.

Both circulars will come into force on 1 January 2015.

FINMA endorses Swiss Bankers Association guidelines on treatment of dormant accounts

The FINMA has endorsed the guidelines issued by the Swiss Bankers Association on the treatment of dormant accounts as a minimum standard. The guidelines reflect recent changes in Swiss banking legislation.

The Banking Act and the Banking Ordinance have recently been revised and contain new rules allowing information about dormant accounts to be published. The revised legislation also makes a distinction between 'contact lost to clients' and 'dormancy' and requires dormant assets to be registered on a central registration platform at least once a year.

The point of contact for persons who believe they have a right to claim dormant assets still remains the Swiss Banking Ombudsman. The guidelines will come into force on 1 January 2015.

PBOC consults on bank deposit insurance rules

The People's Bank of China (PBOC) has issued a consultation draft of the 'Bank Deposit Insurance Rules' to seek public comments. The rules are intended to establish and regulate the deposit insurance system and protect the legitimate rights and interests of depositors. They are also viewed as an important step to establishing the bankruptcy system for financial institutions in China.

The rules will apply to all the PRC-established commercial banks, rural cooperative banks, rural credit cooperatives and other banking financial institutions that take deposits (covered institutions), but generally will not apply to the domestic branches of foreign banks or the overseas branches of Chinese banks.

Under the rules:

- the State Council will designate a deposit insurance funds regulator which will formulate rules on the applicable rate of the insurance premium and all covered institutions shall pay the premium accordingly to this regulator every six months;
- the insurance limit of the principal and interest of the same depositor at one covered institution shall be RMB 500,000 and the excess portion shall be recovered from the liquidated estate of the relevant institution; and
- the insurance deposit funds regulator will be responsible for making repayments to depositors within the insurance limit.

The consultation period will end on 30 December 2014.

SSE issues guidelines on asset-backed securities

The Shanghai Stock Exchange (SSE) has issued the 'Guidelines for Asset-backed Securitisation Business', which are intended to promote the development of asset-backed securitisation and complement the relevant measures on asset-backed securitisation issued by the China Securities Regulatory Commission. The guidelines clarify the detailed requirements on listing, investor suitability and information disclosure for assets-backed securities (ABS). Amongst other things, under the guidelines:

- subsidiaries of securities companies and fund management companies which are qualified to carry out specific client asset management business, can launch asset-backed specific asset management schemes or other special purpose vehicles, and apply for the listing of ABS on SSE;
- in order to be listed on SSE, among other requirements, eligible ABS (i) should have been launched and filed according to the applicable regulation; (ii) have underlying assets that can produce an independent and predictable cash flow; (iii) have a proper trading structure and risk control measures; and (iv) satisfy SSE's requirements on investor suitability management;
- the maximum number of holders for an issue of ABS is 200 and the minimum trade size is RMB 1 million;
- among other qualified institutional investors, qualified foreign institutional investors (QFIIs) and RMB qualified foreign institutional investors (RQFIIs) are qualified to trade ABS on SSE;
- managers, custodians and other disclosure obligors should submit the relevant reports and/or disclose the required information according to the guidelines and other regulations upon initial listing as well as on an on-going basis; and
- SSE supports both spot trading and repurchase agreements for ABS.

SZSE revises guidelines on asset-backed securities

The Shenzhen Stock Exchange (SZSE) has revised the 'Guidelines for Asset-backed Securitisation Business' in order to coordinate with the relevant measures issued by the China Securities Regulatory Commission (CSRC) and adapt them to the new filing system for the asset-backed securitisation programme.

Amongst other things, under the revised guidelines:

- subsidiaries of securities companies and fund management companies which are qualified to carry out specific client asset management business, can launch asset-backed specific asset management schemes or other special purpose vehicles, and apply for the listing of assets-backed securities (ABS) on SZSE;
- in order to be listed on SZSE, the relevant ABS should satisfy the following requirements: (i) the underlying assets should comply with the applicable laws and regulations and a negative list, have clear ownership, and can be identified and produce an independent and predictable cash flow; and (ii) the structure complies with CSRC's requirements as well as the guidance;
- the maximum number of holders for an issue of ABS is 200 and the minimum trade size is RMB 1 million; and
- among other qualified institutional investors, qualified foreign institutional investors (QFIIs) and RMB qualified foreign institutional investors (RQFIIs) are qualified to trade ABS on SZSE.

The guidelines also emphasise the need for information disclosure and clarify the information disclosure requirements on initial listing and follow-up credit rating.

CBRC publishes measures on financial asset management companies

The China Banking Regulatory Commission (CBRC) has published the 'Measures on the Administration and Regulation of Financial Asset Management Companies' which it jointly adopted with the Ministry of Finance, the People's Bank of China, the China Insurance Regulatory Commission (CIRC) and the China Securities Regulatory Commission (CSRC) on 14 August 2014. The Measures include detailed requirements on corporate governance, risk control, management of internal transactions, special purpose vehicles, capital adequacy, financial stability, and information resource management and disclosure. The following aspects are worth noting:

- the Measures regulate financial asset management companies at group level. 'Group' refers to a group of companies consisting of a financial asset management company (the Parent Company), its subsidiaries, special purpose vehicles and other affiliated entities. Non-regulated subsidiaries of the Group are regulated indirectly through the Parent Company, while regulators coordinate with each other to comprehensively regulate regulated subsidiaries of the Group;
- a Group's shareholding structure is required to be controlled within three layers (unless for the purpose of complying with financial regulations);
- certain intra-group transactions are prohibited by the Measures;
- the minimum capital adequacy ratio of a Parent Company is 12.5%;
- the capital of a Parent Company, its banking subsidiaries and its non-financial institution subsidiaries is subject to the capital requirement relating to consolidation as imposed by the CBRC; and
- the Measures also regulate the group supplement capital of a Group, which is (i) the aggregation of all accredited capital of the Parent Company and financial institution subsidiaries (by multiplying shareholding ratio) less (ii) (A) the amount of capital held between subsidiaries and held by subsidiaries in the Parent Company, and (B) capital that is confirmed to be not transferrable.

The Measures will take effect on 1 January 2015.

HKMA issues circular on stable funding requirement

The Hong Kong Monetary Authority (HKMA) has issued a circular on the stable funding requirement (SFR), which was introduced in October 2013 and required authorised institutions (AIs) with significant loan growth to ensure adequate stable funding to support their lending business from 2014 onwards. To streamline the SFR's operation and alleviate AIs' reporting burden, the HKMA has conducted a review and has sought industry associations' input. The HKMA will implement several refinements to the SFR with effect from January 2015. These refinements include, among other things, the following:

- AIs with total loans of HKD 10 billion or more and annualised average loan growth in the latest eight quarters exceeding 15% will be required to observe the SFR;
- the frequency of review and report submission will be changed to quarterly;
- the SFR ratio applicable to an AI, subject to a cap of 100%, for calculating the stable funding to be obtained will be based on the AI's quarterly loan growth rate; and
- subject to certain caps and conditions, additional flexibility will be allowed for exempting loans and

accepting Head Office's irrevocable committed liquidity facility as stable funding.

A comparison between the existing and refined SFR regime is included at Annex 1 of the circular. Illustrations of SFR calculation based on the refined regime are at Annex 2 of the circular.

The HKMA has indicated that, similar to the existing arrangement, AIs that fall within the thresholds set out above will be given two months after each quarter end to achieve compliance if they are required to obtain additional stable funding. Thereafter, the applicability of the SFR to AIs, including those AIs not yet falling within the thresholds, would be reviewed on a quarterly basis. While the SFR is and will continue to be only applicable to AIs meeting certain loan portfolio and credit growth thresholds, the HKMA may, on a case by case basis, require an AI to maintain a higher level of SFR ratio or require an AI outside of the scope of the SFR to observe the SFR if the HKMA is not satisfied with the quality of its liquidity risk management or is concerned with its arrangements which, in the HKMA's view, are for the purpose of limiting the HKMA's supervisory reach by circumventing the SFR.

Starting from the end of December 2014 position, every AI meeting the revised thresholds should submit quarterly reports in the format set out at Annex 3 to the HKMA's private website within 14 calendar days after each quarter end. The first reporting deadline will be 14 January 2015.

MAS publishes Notice 649 on minimum liquid assets and liquidity coverage ratio for banks

The Monetary Authority of Singapore (MAS) has published a new Notice 649 on Minimum Liquid Assets and Liquidity Coverage Ratio, along with the responses to its August 2014 consultation paper on a draft MAS Notice on the Liquidity Coverage Ratio (LCR) requirement for banks in Singapore and proposed revisions to the Minimum Liquid Assets (MLA) requirement.

The new MAS Notice 649 incorporates the revised liquidity framework for banks.

Amongst other things, the MAS has confirmed that:

- regarding the criteria for country-level compliance with the LCR requirement, it will assess whether a group of banks applying for country level compliance does in fact manage their liquidity risk on a consolidated basis;
- it will not be making further changes to the high-quality liquid assets (HQLA) haircuts, nor the outflow and inflow factors, under the LCR requirement set out in MAS Notice 649;
- additional language has been included in paragraph 6 of MAS Notice 649 to clarify that liabilities due to intragroup banking entities will be included in the computation of qualifying liabilities;
- MAS Notice 649 will replace MAS Notice 613 in two stages. Specifically, MAS Notice 649 will apply to banks incorporated and headquartered in Singapore from 1 January 2015, and all other banks from 1 January 2016. MAS Notice 640 on Asset Maintenance will not be affected. MAS Notice 758 on Minimum Cash Balance will be amended to include the definition of Qualifying Liabilities under MAS Notice 649 instead of referencing MAS Notice 613, which will be cancelled with effect from 1 January 2016; and
- the equivalent liquidity rules for finance companies and merchant banks will be released in 2015 – the proposed rules will be subject to a public consultation period prior to finalisation, and there will be a transition period for affected entities to comply with the new requirements.

RECENT CLIFFORD CHANCE BRIEFINGS

Reflections from the International Arbitration Group

In this publication, Clifford Chance international arbitration practitioners from across our global network – in the UK, Europe, Middle East, Asia Pacific and the Americas – comment on significant trends and developments in the field of International Arbitration.

Their views are wide ranging and varied, reflecting the broad range of issues that organisations involved in international arbitration face today.

http://www.cliffordchance.com/briefings/2014/12/reflections_fromtheinternationalarbitratio.html

Real estate finance – identifying common pitfalls and solutions

As the real estate finance market has returned to strength over the last two years, the London property market has boomed and spreads have continued to tighten, it is easy to lose sight of the protections needed should things go wrong.

In this article, Clifford Chance experts provide an overview of the current market, examine whether some of the important lessons of downturn risk have been forgotten, and provide reminders on best practice structuring and documentation points.

http://www.cliffordchance.com/briefings/2014/12/real_estate_financeidentifyingcommonpitfall.html

HKMA and SFC Consultation Conclusions pave way for mandatory reporting of OTC derivatives in Hong Kong in 2015

The Hong Kong Monetary Authority (HKMA) and the Securities and Futures Commission (SFC) have released their consultation conclusions in relation to the proposed reporting and record keeping rules in respect of OTC derivative transactions. In a welcome development for the fund management industry and end users, the HKMA and SFC have decided to adopt a phased approach to the introduction of mandatory reporting of OTC derivatives in Hong Kong, with dealers being the first category of market participants to be subject to the reporting requirements. The revised Rules applicable to dealers are expected to come into effect in the first quarter of 2015, with a six month grace period before mandatory reporting commences.

The regulators have made a number of amendments to the Rules after consideration of market feedback, such as an extension of the grace period, clarification of the product scope and broadening the availability of data masking.

This briefing sets out observations on the revised Rules contained in the Consultation Conclusions and highlights the key developments that market participants should be aware of for 2015.

http://www.cliffordchance.com/briefings/2014/12/hkma_and_sfc_consultationconclusionspavewa.html

Partnerships and companies – new rules on registration of capital

The Central Partnership and Company Registration Office has issued new rules for partnerships and companies registering either their initial capital or an additional capital increase by an amount exceeding Baht 5 million.

This briefing discusses the new rules.

http://www.cliffordchance.com/briefings/2014/12/thailand_partnershipsandcompaniesnewrule.html